



DEPARTMENT OF THE TREASURY

INTERNAL REVENUE SERVICE

1100 Commerce, MC 4920 DAL

Dallas, TX 75242

501-04.00

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Release Number: **201335017**

Release Date: **8/30/2013**

LEGEND

ORG - Organization name

XX - Date Address - address

Date: **May 1, 2013**

Taxpayer Identification Number:

Form:

Tax Year(s) Ended:

Person to Contact/ ID Number

Contact Numbers:

Phone:

Fax

CERTIFIED MAIL - RETURN RECEIPT REQUESTED

Dear :

In a determination letter dated March 11, 19XX, you were held to be exempt from Federal income tax under section 501(c)(4) of the Internal Revenue Code (the Code).

Based on recent information received, we have determined you have not operated in accordance with the provisions of section 501(c)(4) of the Code. Accordingly, your exemption from Federal income tax is revoked effective January 1, 20XX. This is a final letter with regard to your exempt status.

We previously provided you a report of examination explaining why we believe revocation of your exempt status was necessary. At that time, we informed you of your right to contact the Taxpayer Advocate, as well as your appeal rights. On February 27, 20XX you signed Form 6018-A, Consent to Proposed Action, agreeing to the revocation of your exempt status under section 501(c)(4) of the Code.

You are required to file Federal income tax returns for the tax period(s) shown above. If you have not yet filed these returns, please file them with the Ogden Service center within 60 days from the date of this letter, unless a request for an extension of time is granted. File returns for later tax years with the appropriate service center indicated in the instructions for those returns.

You have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and

proper handling. You may call toll-free, 1-877-777-4778, and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

If you have any questions, please contact the person whose name and telephone number are shown at the beginning of this letter.

Thank you for your cooperation.

Sincerely,

Nanette M. Downing
Director, EO Examinations

Internal Revenue Service
Tax Exempt and Government Entities Division
Exempt Organizations: Examinations
801 Tom Martin Dr. Room 263
Birmingham, AL 35211

Department of the Treasury

Date: February 8, 2013

Taxpayer Identification Number:
Form:
Tax Year(s) Ended:
Person to Contact/ID Number:
Contact Numbers:
Telephone:
Fax:

ORG
ADDRESS

Certified Mail – Return Receipt Requested

Dear .:

We have enclosed a copy of our report of examination explaining why we believe revocation of your organization's exempt status is necessary.

If you do not agree with our position you may appeal your case. The enclosed Publication 3498, *The Examination Process*, explains how to appeal an Internal Revenue Service (IRS) decision. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process.

If you request a conference, we will forward your written statement of protest to the Appeals Office and they will contact you. For your convenience, an envelope is enclosed.

If you and Appeals do not agree on some or all of the issues after your Appeals conference, or if you do not request an Appeals conference, you may file suit in United States Tax Court, the United States Court of Federal Claims, or United States District Court, after satisfying procedural and jurisdictional requirements as described in Publication 3498.

You may also request that we refer this matter for technical advice as explained in Publication 892, *Exempt Organization Appeal Procedures for Unagreed Issues*. If a determination letter is issued to you based on technical advice, no further administrative appeal is available to you within the IRS on the issue that was the subject of the technical advice.

If you accept our findings, please sign and return the enclosed Form 6018, *Consent to Proposed Adverse Action*. We will then send you a final letter revoking your exempt status. If we do not hear from you within 30 days from the date of this letter, we will process your case on the basis of the recommendations shown in the report of examination and this letter will become final. In that event, you will be required to file Federal income tax returns for the tax period(s) shown above. File these returns with the Ogden Service Center within 60 days from the date of

this letter, unless a request for an extension of time is granted. File returns for later tax years with the appropriate service center indicated in the instructions for those returns.

You have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free 1-877-777-4778 and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

If you have any questions, please call the contact person at the telephone number shown in the heading of this letter. If you write, please provide a telephone number and the most convenient time to call if we need to contact you.

Thank you for your cooperation.

Sincerely,

Nanette M. Downing
Director, EO Examinations

Enclosures:
Publication 892
Publication 3498
Form 6018-A
Report of Examination
Envelope

Form 886-A (Rev. January 1994)	EXPLANATIONS OF ITEMS		Schedule number or exhibit
Name of taxpayer	Tax Identification Number	Year/Period ended	
ORG	EIN	20XX & 20XX12	

LEGEND

ORG - Organization name EIN - ein XX - Date State - state Country -
country City - city CO-1, CO-2

Issue:

Whether ORG qualifies for exemption under Internal Revenue Code (IRC) Section 501(c)(4)?

Facts:

The ORG was denied exemption as a 501(c)(7) organization on February 06, 19XX. A letter dated June 3, 19XX requested an appeals review of the 501(c)(7) denial. Appeals issued a letter dated March 11, 19XX granting the ORG exemption as a 501(c)(4) organization. IRC section 501(c)(4) provides for exemption of two very different types of organizations with their own distinct qualification requirements. They are:

- a. "Social welfare organizations"-- Civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare, and
- b. "Local associations of employees" the membership of which is limited to the employees of a designated person(s) in a particular municipality, and the net earnings of which are devoted exclusively to charitable, educational, or recreational purposes.

- (1) To qualify as a local association of employees under IRC section 501(c)(4) the organization must:
- a. Be local in character, its membership must be limited to employees of a designated employer(s) in a particular locality, and
 - b. Devote its net earnings exclusively to charitable, educational, or recreational purposes.

(2) For purposes of the local requirement, Treas. Reg. section 1.501(c)(4)-1(b) refers to the definition of local in Treas. Reg. section 1.501(c)(12)-1(b). For this purpose, business limited only by the borders of a state would not be local.

According to your Articles of Incorporation filed May 26, 19XX the purpose for which this corporation is organized is to operate a center that caters to the particular recreational and social needs of the crew members of cruise ships docking at the Port of State, and to conduct incidental activities related thereto, including but not limited to the maintenance and operation of any park with recreational facilities adjacent to facilities of the organization. This corporation shall carry on no activities which are not permitted to be carried on by an organization exempt from federal income tax under section 501(c)(7) of the Internal Revenue Code of 1986 or the corresponding provision of any future United States Internal Revenue Law. In the event of dissolution, the residual assets of this corporation will be turned over to one or more organization which are exempt as organizations described in section 501(c)(3) and 170(c)(2) of the Internal Revenue Code of 1986 or corresponding sections of any prior or future Internal Revenue Code, or to the Federal, State or local government for exclusive public purposes.

During the examination of your Form 990 for 20XX and 20XX you were asked during the initial interview to describe the history of your organization and all of its activities. You stated that "the CO-1 closed their operations back in the late 80s. ORG was established to continue to offer service to seafarers working on ships calling on Port of State. The service consisted of, low cost phone calls to families at home, this later turned into Internet service, etc. mailing service, money transfer and food were also available. Sport

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activities were arranged and the center also had a soccer field in the earlier days. That area was later taken by the port. In addition, ORG manages the buildings where the services are provided."

You were asked does the organization own, lease or sublease any real property. If so, is the property encumbered by debt? You responded "ORG owns three modular buildings which are located on City property. The center pays ground lease to the Port of State for use of the grounds that the buildings are on. The buildings were sold in October 20XX. ORG has no outstanding debt."

According to your 20XX and 20XX Form 990 you received income from the following sources:

TABLE DELETED

The 1024 application stated that the source of income would be net income from telephone services, food service and sundry shop. It also stated the miscellaneous gifts from cruise and shipping and governmental welfare organization would also be a source of income. However during the examination it was noted that the only source of income was rental income and ships per call fees. Your explanation of ship per calls fees is "the center, which was originally founded by the Country Government, who pulled out back in the 19XXs, The ORG was created to operate the facility going forward. The two major Country cruise lines that operated out of the Port of State, had a large number of their crew being from Country, therefore, the two cruise lines paid \$ per ship, per call to the center as a way of supporting their efforts of the ORG. CO-2 pulled out several years ago, and Country Cruise Lines pulled out a year ago."

According to your 20XX and 20XX Form 990 you listed expenses of the following:

TABLE DELETED

The expenses listed above appear to be commercial in nature and as a 501(c)(4) "Local associations of employees" the membership of which is limited to the employees of a designated person(s) in a particular municipality, and the net earnings of which are devoted exclusively to charitable, educational, or recreational purposes. The expenses listed above are not commensurate with that of a 501(c)(4) organization.

Law:

Treas. Reg. 1.501(c)(4)-1(d)

(b) Local associations of employees. Local associations of employees described in section 501(c)(4) are expressly entitled to exemption under section 501(a). As conditions to exemption, it is required (1) that the membership of such an association be limited to the employees of a designated person or persons in a particular municipality, and (2) that the net earnings of the association be devoted exclusively to charitable, educational, or recreational purposes. The word local is defined in paragraph (b) of § 1.501(c)(12)-1. See paragraph (d)(2) and (3) of § 1.501(c)(3)-1 with reference to the meaning of charitable and educational as used in this section.

(b) The phrase of a purely local character applies to benevolent life insurance associations, and not to the other organizations specified in section 501(c)(12). It also applies to any organization seeking exemption on the ground that it is an organization similar to a benevolent life insurance association. An organization of a purely local character is one whose business activities are confined to a particular community, place, or

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district, irrespective, however, of political subdivisions. If the activities of an organization are limited only by the borders of a State it cannot be considered to be purely local in character.

(2) Charitable defined. The term charitable is used in section 501(c)(3) in its generally accepted legal sense and is, therefore, not to be construed as limited by the separate enumeration in section 501(c)(3) of other tax-exempt purposes which may fall within the broad outlines of charity as developed by judicial decisions. Such term includes: Relief of the poor and distressed or of the underprivileged; advancement of religion; advancement of education or science; erection or maintenance of public buildings, monuments, or works; lessening of the burdens of Government; and promotion of social welfare by organizations designed to accomplish any of the above purposes, or (i) to lessen neighborhood tensions; (ii) to eliminate prejudice and discrimination; (iii) to defend human and civil rights secured by law; or (iv) to combat community deterioration and juvenile delinquency. The fact that an organization which is organized and operated for the relief of indigent persons may receive voluntary contributions from the persons intended to be relieved will not necessarily prevent such organization from being exempt as an organization organized and operated exclusively for charitable purposes. The fact that an organization, in carrying out its primary purpose, advocates social or civic changes or presents opinion on controversial issues with the intention of molding public opinion or creating public sentiment to an acceptance of its views does not preclude such organization from qualifying under section 501(c)(3) so long as it is not an action organization of any one of the types described in paragraph (c)(3) of this section.

(3) Educational defined--(i) In general. The term educational, as used in section 501(c)(3), relates to:

- (a) The instruction or training of the individual for the purpose of improving or developing his capabilities; or
- (b) The instruction of the public on subjects useful to the individual and beneficial to the community.

An organization may be educational even though it advocates a particular position or viewpoint so long as it presents a sufficiently full and fair exposition of the pertinent facts as to permit an individual or the public to form an independent opinion or conclusion. On the other hand, an organization is not educational if its principal function is the mere presentation of unsupported opinion.

Reg. 1.274-2(f)(2)(v) provides that expenditures that are deductible by employers because they are for employee recreational activities include expenditures for Christmas parties, picnics, summer outings, a swimming pool, a baseball diamond, bowling alleys and a golf course.

Revenue Procedure 80-25, 1980-1 CB 667, Section 12.02 states that a ruling or determination letter recognizing exemption may not be relied upon if there is a material change, inconsistent with exemption, in the character, the purpose, or the method of operation of the organization. Sec 13.01 further states that where there is a material change, inconsistent with exemption, in the character, the purpose, or the method of operation of an organization, revocation or modification will ordinarily take effect as of the date of such material change.

Section 13.01 states that a ruling or determination letter recognizing exemption may be revoked or modified by a subsequent ruling or determination letter addressed to the organization, or by a revenue ruling or other statement published in the Internal Revenue Bulletin. The revocation or modification may be retroactive if the organization omitted or misstated a material fact, operated in a manner materially different from that originally represented, or, in the case of organizations to which section 503 of the Code applies, engaged in a prohibited transaction with the purpose of diverting corpus or income of the organization from its

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exempt purpose and such transaction involved a substantial part of the corpus or income of such organization. Where there is a material change, inconsistent with exemption, in the character, the purpose, or the method of operation of an organization, revocation or modification will ordinarily take effect as of the date of such material change. In cases where a ruling or determination letter was issued in error or is no longer in accord with the holding of the Service, retroactivity of the revocation or modification ordinarily will be limited to a date not earlier than that on which the original ruling or determination letter is modified or revoked.

Revenue Procedure 2007-52, Section 12.01(1) states that where there is a material change, inconsistent with exemption, in the character, the purpose, or the method of operation of an organization, revocation or modification will ordinarily take effect as of the date of such material change.

Governments Position:

An organization exempt under IRC 501(c)(4) Civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare, or local associations of employees, the membership of which is limited to the employees of a designated person or persons in a particular municipality, and the net earnings of which are devoted exclusively to charitable, educational, or recreational purposes; shall not apply to an entity unless no part of the net earnings of such entity inures to the benefit of any private shareholder or individual.

The ORG no longer qualifies for exemption as a 501(c)(4) organization because the net earnings are not devoted exclusively to charitable, educational, or recreational purposes of its members. The organizations main source of income is rental income and expenses are related to the upkeep of these rented facilities. During the years under examination the organization did not conduct any activities for its members as illustrated in the tables above. The organization appears to be operating in a commercial nature. As stated above if there were a material change, inconsistent with exemption, in the character, the purpose, or the method of operation of an organization, revocation or modification will ordinarily take effect as of the date of such material change. The organization is no longer operating within the guidelines of IRC 501(c)(4) and therefore no longer qualify for exemption.

Taxpayers Position:

The ORG will have an opportunity to respond once this report is received.

Conclusion:

The IRC Section 501(c)(4) tax exempt status of ORG should be revoked since the organization is no longer providing any exempt services to its members. A material change has taken place which is inconsistent with exemption, in character, and in purpose and therefore your 501(c)(4) should be revoked.